# Discussion of “Knowing What Not To Do: Financial Literacy and Consumer Credit Choices,” “Financial Literacy and High-Cost Borrowing in the United States,” and “Effect of Monitoring on Mortgage Delinquency”


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# Overview

- Broad theme: The effect of financial literacy/capability on financial well-being and financial behaviors
- Jaroszek and Lusaridi both use measures of financial knowledge to examine the effect of financial literacy on use of high-cost credit
- Moulton examines the effect of providing financial coaching to homebuyers on default

# Summary: Jaroszek and Dick

- Use household panel data from Germany that includes measures of financial literacy, numeracy, self-control, and use of high cost credit (overdraft)
- Higher financial literacy reduces use of overdraft
- Low self-control increases probability of using high cost credit by 20 percent
- Financial literacy can compensate for low self-control

# Comments

- Extremely well done paper
  - Use novel measures of self-control, control for numeracy
  - Present the effects of financial literacy, numeracy, and self-control on overdraft use several ways
  - Robustness check using different empirical approach and also controlling for being credit constrained
- Good to see similar findings in both the German and US data

# Comments

- Earlier draft made use of question about how quickly people spent pocket money as a child
  - Only available for subset and some problems with reporting, but find that quick spending is strongly associated with use of overdraft
- Earlier draft also had robustness check using factor analysis to generate financial literacy index that yielded similar findings
  - Consider adding back in

# Summary: Lusardi and Scheresberg

- Use FINRA Foundation's 2009 National Financial Capability Study to examine use of payday loans, auto title loans, RALs, pawn shops, and rent-to-own stores (collectively AFS)
- Examine relationship between financial literacy and use of AFS
  - Difference between highest and lowest level of literacy ≈20% reduction in probability of using AFS
  - Financial literacy effect is robust to inclusion of demographics, risk tolerance, and measures of vulnerability

# Comments

- Adds to Anna's already extensive work demonstrating that low financial literacy is associated with negative financial behaviors and outcomes
  - Evidence on the credit side instead of asset side
- Provides detailed information on AFS users
- Discusses how a wide range of variables affect use of AFS in regression context

# Comments

- Sampling design was extremely complex and non-traditional
  - Two different opt-in internet panels
  - Use of state by state quotas (race, age, etc.)
  - Population weights are not sufficient to yield representative estimates
- Additional comparison to National Survey done by RDD would support the State Survey numbers
- Looking forward to comparison with 2012 survey

# Summary: Collins et al.

- Use RCT to examine the effect of telephone financial coaching for first-time homebuyers on default, savings, debt levels, auto-pay
- Coaching reduces default among low-credit score borrowers (<680)
  - 30-40% reduction in default probability from 9-20 phone calls! (≈10 percentage points)
- No significant effect on high score borrowers
- Significantly increases use of auto-pay
- Higher reported saving

# Comments

- Hard to criticize a RCT
  - Random assignment
  - Samples balanced
  - Results robust to including controls and using IV
- Given varying lengths of observation for borrowers supplement with standardized outcome if feasible (e.g. 12 month default rate)
- Many different time periods
  - Figure showing dates of recruitment, treatment, data collection, etc. would be useful
- Discuss costs vs. benefits (I imagine these calls were extremely low cost relative to default)

# Policy Implications

- Strong evidence that some underlying financial literacy factor is an important determinant of nearly every aspect of household financial well-being
- Problem is translating that knowledge into effective interventions that actually improve underlying financial literacy and thus financial outcomes
  - Not enough to teach people the answers to Big 3 or Big 5 questions
  - Mixed evidence on effectiveness of financial education
  - Additional research needed evaluating specific programs (education and interventions) so that we know what works and what doesn't (and for whom)
  - Also know what is and is not cost effective

# Effectiveness of Interventions

- Moulton demonstrates that a timely and targeted intervention can improve financial outcomes
  - However only works for low-credit score (low financial literacy?) individuals
- Increasing number of studies showing the effectiveness of these types of targeted interventions
  - Savings reminders (Kast et al. 2012)
  - Foreclosure counseling (Collins and Schmeiser 2012)

# Effectiveness of Financial Education

Georgia:

In 2004 State Board of Education approved the new Georgia Performance Standards (GPS) Social Studies Curriculum which strengthens economics content across K-8 grades and explicitly includes Personal Finance in all grades, including high school beginning Fall 2006 (Source: Jump$tart)

# Georgia Results

| | (1) | (2) |
|---|---|---|
| | Credit Score | Account 60 Plus Days Delinquent |
| Fin Lit (Implementation) | 3.959*** | -0.0157*** |
| | (0.765) | (0.00463) |
| Fin Lit (One Year Post) | 4.282*** | -0.0182*** |
| | (0.821) | (0.00503) |
| Fin Lit (Two Years Post) | 5.722*** | -0.0240*** |
| | (0.914) | (0.00560) |
| Fin Lit (Three Years Post) | 6.544*** | -0.0236*** |
| | (1.075) | (0.00646) |
| Fin Lit (Four Years Post) | 7.189*** | -0.0202** |
| | (1.364) | (0.00788) |
| Fin Lit (Five Years Post) | 11.10*** | -0.0339*** |
| | (2.013) | (0.0107) |
| Observations | 330494 | 371123 |

# Conclusions

- Importance of financial literacy widely acknowledged
- These papers yield further evidence that financial literacy affects outcomes independent of numeracy, demographics, self-control, etc.
- Interventions can be effective (at least for certain populations) and perhaps compensate for low financial literacy
- Education may be effective but much research to do before we know what types and topics yield the greatest benefit